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YOUR TAXES HAVE BEEN GOING UP: CONSUMPTION TAX INCREASES

June 1987

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WHY YOUR TAXES HAVE BEEN GOING UP: CONSUMPTION TAX INCREASES

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WHY YOUR TAXES HAVE BEEN GOING UP: FEDERAL CONSUMPTION TAX INCREASES

Budget Changes

Everyone knows that governments raise revenue through income tax. However, few Canadians are aware that they also pay 'hidden taxes' in the form of federal sales and excise taxes and duties. Recent federal budgets have imposed increases in federal sales and excise taxes, also known as 'consumption taxes' or 'commodity taxes'. These tax hikes have hit low-income Canadians hardest.

Ottawa levies a **sales tax** on goods manufactured in Canada or imported into Canada. However, all services and exports are exempt as well as a range of items including food, clothing, footwear, prescription drugs, electricity and fuels, materials used in manufacturing, construction equipment, bicycles, farming and mining machinery. Leading sources of federal sales tax revenue include gasoline and diesel fuel, motor vehicles and parts, alcohol and tobacco, construction materials and furniture.

In addition to the sales tax, the federal government charges **excise taxes** on certain domestic and imported goods, including wine, cigars and cigarettes, tobacco, air conditioners in motor vehicles, automotive and aviation fuel, large cars and jewellery. It also levies **excise duties** on domestically-produced alcoholic beverages and tobacco products.

Federal and provincial income taxes, provincial sales tax and municipal property taxes are 'visible' taxes because their amount is made known to taxpayers, consumers and homeowners. However, federal sales and excise taxes are 'hidden' or 'invisible' taxes because they are not itemized separately on the consumer's bill. Instead, federal commodity taxes are built into the final price of the goods to which they apply.

Over the past several years, Finance Minister Wilson has announced successive increases in sales and excise taxes and duties. In November 1984, he raised the federal sales tax from 5 to 6 percent on construction materials and equipment for buildings, from 12 to 13 percent on alcoholic beverages and tobacco and from 9 to 10 percent on other taxable goods for the period October 1, 1984 to December 31, 1988. He also broadened the sales tax to include cable and pay television services.

The May 1985 Budget extended these federal sales tax increases beyond the December 31, 1988 termination date. It also raised the sales tax by another percentage point (i.e., to 7 percent on construction material and cable and pay television services, 14 percent on alcoholic beverages and tobacco and 11 percent on other taxable goods). The scope of the federal sales tax was widened to cover a number of consumer goods that previously were exempt - candy and confectionery, pet foods, soft drinks, health goods (e.g., medicated creams, lotions, shampoo, soaps and bandages), surgical instruments and insulation materials, among others. The government increased the excise tax on motive fuels by 2 cents per litre, on cigarettes and on alcoholic beverages by 2 percent.

The February 1986 Budget raised the federal sales tax by another percentage point effective April 1, 1986. Excise taxes and duties on alcohol went up by 4 percent and on tobacco products by 6 percent as of February 27, 1986. The latter increases translated into tax hikes of about 12 cents on a 710 ml bottle of liquor, 1 cent on a 750 ml bottle of wine, 6 cents for a case of 24 beer and 4.5 cents for a pack of 25 cigarettes.

The February 1987 Budget brought another round of commodity tax increases. The federal sales tax was extended to certain snack foods such as potato chips, salted nuts, popped corn and granola bars, as of July 1, 1987. The excise tax on gasoline and diesel fuel went up by 1 cent a litre on February 19, 1987. Excise taxes and duties on cigarettes and other tobacco products increased by 4 percent.

The Effects of Commodity Tax Increases

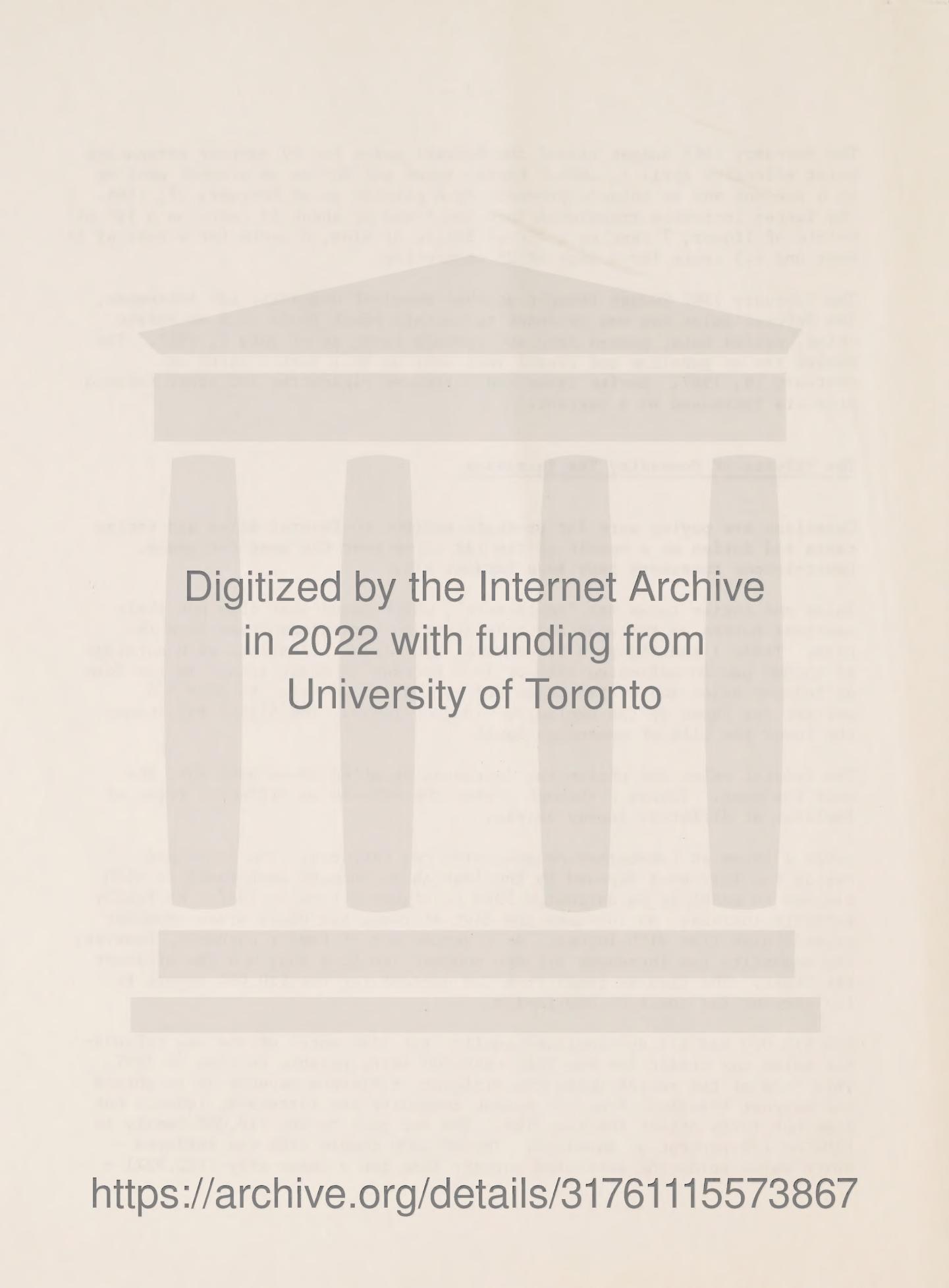
Canadians are paying more for products subject to federal sales and excise taxes and duties as a result of the tax hikes over the past few years. Lower-income consumers have been hardest hit.

Sales and excise taxes are 'regressive', which means that they put their heaviest burden on the poor and take least in percentage terms from the rich. Table 1 and Figure A illustrate this effect. Families with earnings of \$5,000 pay an estimated \$980 or 14.4 percent of their income in the form of federal sales and excise taxes and duties, in contrast to only 4.4 percent for those at the exclusive \$100,000 level. The higher the income, the lower the bite of commodity taxes.

The federal sales and excise tax increases detailed above have hurt the poor the most. Tables 2 through 4 show the effects on different types of families at different income levels.

Table 2 looks at two-earner couples with two children. The sales and excise tax increases imposed by the last three budgets cost families with \$10,000 in earnings an estimated \$344 in higher prices in 1987. As family earnings increase, so too does the cost of these tax hikes since consumer expenditures rise with income. As a percentage of family earnings, however, the commodity tax increases hit the poorest families most and the affluent the least. The figures range from 2.4 percent for the \$20,000 couple to 1.1 percent for the \$100,000 family.

The \$10,000 and \$15,000 families qualify for \$150 worth of the new refundable sales tax credit for the 1986 taxation year, payable to them in 1987. This form of tax relief which the Minister of Finance brought in to shield the poorest Canadians from his recent commodity tax increases, reduces but does not fully offset the tax hike. The net cost to the \$10,000 family is \$194 or 1.9 percent of earnings. The \$20,000 couple with two children - which earns below the estimated poverty line for a large city (\$22,532) -



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faces the highest federal commodity tax increase (2.4 percent of earnings) because it does not qualify for the sales tax credit.

The other tables paint a similar picture: **Federal consumption tax increases over the past few years have hit the poor the hardest. The new sales tax credit partially shelters the poorest Canadians from these tax hikes but does not help the working poor who are over the \$15,000 income limit for the maximum credit but still remain below the poverty line.**

Table 1

Estimated Impact of Federal Consumption Taxes, Families With Two Children, by Earnings, 1987

Family Earnings	Family Income	Estimated Consumption Taxes	Consumption Taxes As Per Percentage of Income
\$ 5,000	\$ 6,826	\$ 980	14.4%
10,000	11,826	1,372	11.6
15,000	16,826	1,678	10.0
20,000	21,676	1,939	8.9
25,000	26,676	2,172	8.1
30,000	31,473	2,384	7.6
40,000	41,011	2,765	6.7
50,000	50,768	3,105	6.1
75,000	75,768	3,840	5.1
100,000	100,768	4,473	4.4

Note

1. Federal consumption taxes are sales tax and excise taxes and duties.
2. Family income includes (where applicable) family allowance, child tax credit and sales tax credit.

Figure A
Estimated Federal Consumption Taxes as Percentage of Income,
Families With Two Children, by Earnings, 1987

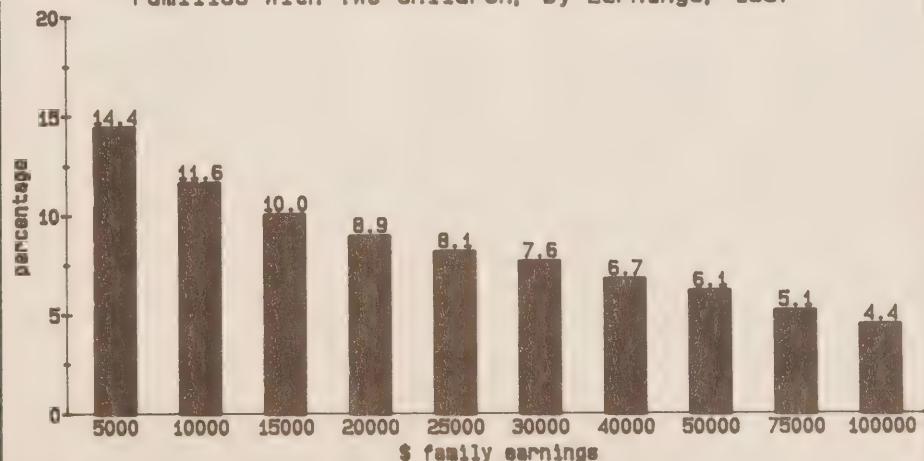


Table 2

Estimated Impact of 1985-1987 Budgets' Changes to Federal Consumption Taxes, Two Earner Couples With Two Children, by Family Earnings, 1987

Family Earnings	Estimated Consumption Tax Increase	Sales Tax Credit	Net Increase	As Percentage of Family Earnings
\$ 10,000	\$ 344	\$150	\$ 194	1.9%
15,000	420	150	270	1.8
20,000	484	0	484	2.4
25,000	540	0	540	2.2
30,000	592	0	592	2.0
40,000	684	0	684	1.7
50,000	766	0	766	1.5
75,000	933	0	933	1.2
100,000	1,082	0	1,082	1.1

Table 3

Estimated Impact of 1985-1987 Budgets' Changes to Federal Consumption Taxes, One-Earner Couples With Two Children, by Family Earnings, 1987

Family Earnings	Estimated Consumption Tax Increase	Sales Tax Credit	Net Increase	As Percentage of Family Earnings
\$ 10,000	\$ 353	\$150	\$ 203	2.0%
15,000	424	150	274	1.8
20,000	483	0	483	2.4
25,000	534	0	534	2.1
30,000	581	0	581	1.9
40,000	663	0	663	1.7
50,000	735	0	735	1.5
75,000	882	0	882	1.2
100,000	1,010	0	1,010	1.0

Table 4

Estimated Impact of 1985-1987 Budgets' Changes to Federal Consumption Taxes, Single Parent With Two Children, by Family Earnings, 1987

Family Earnings	Estimated Consumption Tax Increase	Sales Tax Credit	Net Increase	As Percentage of Family Earnings
\$ 5,000	\$ 121	\$100	\$ 21	0.4%
10,000	214	100	114	1.1
15,000	299	0	299	2.0
20,000	378	0	378	1.9
25,000	456	0	456	1.8
30,000	530	0	530	1.8

